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SUBJECT: BOUTEFLIKA MULLS CHANGES TO 2005 HYDROCARBON LAW

REF: ALGIERS 1247

SUMMARY

¶1. (SBU) President Bouteflika is reviewing proposed changes to Algeria's 2005 hydrocarbon law, touted at the time as a major step toward greater openness. The proposed changes would slow down current rates of oil and gas exploitation while limiting the expanded role for foreign energy companies established in last year's legislation. Although details of the changes are not yet confirmed, Bouteflika voiced his support for the establishment of strategic energy reserves that would benefit future generations of Algerians. Such changes, while criticized by one Sonatrach executive as imparting a negative image of Algeria to potential investors, would nonetheless likely come as a relief to elements of the Algerian public that were highly critical of the share accorded to foreign investors under the 2005 law. The amendments would also be a defeat for Energy Minister Khelil, who was seen as the primary architect of the 2005 legislation, and a possible setback for economic reform. (End Summary.)

PRESIDENT WOULD BYPASS PARLIAMENT

¶2. (U) President Bouteflika is reviewing proposed changes to Algeria's 2005 hydrocarbon law that would limit the recently expanded role of foreign energy companies in Algeria and would establish strategic reserves to benefit future generations of Algerians. By waiting until the parliamentary recess, which began July 9, Bouteflika can pass the changes as an executive order, thereby circumventing Parliament. He would have until the first Tuesday of October, when Parliament reconvenes, to sign his decision into law.

NEW AMENDMENTS WOULD AUGMENT SONATRACH'S ROLE

¶3. (U) While details of the proposed amendments are not yet confirmed, Embassy contacts said the amendment would maintain Sonatrach's right from before the 2005 law to hold 51 percent of upstream projects. (The 2005 law lowered this figure to a range from 20 to 30 percent while giving Sonatrach the choice to join with foreign partners; the new amendments would make Sonatrach's participation obligatory.) Although the 2005 hydrocarbon law was adopted by presidential decree in April 2005 and became law with its July 2005 publication in the official gazette, Embassy contacts at Sonatrach confirmed that the law was never officially implemented. Therefore, no contracts subject to its sharing agreements have been signed. (The last international licensing round of tenders for

upstream projects ended just prior to the adoption of the new law, in March 2005.) Post has no details of the proposed "strategic energy reserves," although one U.S. energy firm's country manager told Econoff that he had heard rumors Sonatrach was reserving some 60 exploration blocks for its own exploitation.

¶4. (U) Embassy contacts in the U.S. business community note that the new amendment is also expected to change the tax structure for foreign firms, although the formula for doing so is far from clear. Prior to the 2005 legislation, taxes paid to the state were included in the 51 percent share accorded to Sonatrach. Meanwhile, the reference price used to calculate foreign firms' tax liabilities was locked in at USD 19 per barrel. In a press conference July 15, Minister of Energy and Mines Chakib Khelil said that taxes for foreign firms would increase as long as the price of oil exceeded USD 30 per barrel. The official government daily El Moudjahid reported July 16 that this would translate into a 40 percent tax hike for foreign firms (30 percent paid to the GoA and 10 percent paid to their country of origin), yet the calculation for these figures is still not clear. Contacts in the U.S. business community were equally perplexed. One country manager for a U.S. energy company told Econoff that he and his colleagues had no idea how the taxation structure would change, such as whether taxes would be included in Sonatrach's 51 percent (as before) or come out of the foreign partner's 49 percent. He noted, however, he and his colleagues were less anxious about the sanctity of current contracts than the impact of the amendments on future projects.

¶5. (U) Advocates of the amendments insist that they do not

invalidate the main thrusts of the 2005 law and that they are simply a recalibration in light of record-high energy prices. Specifically, at this point, the amendments do not seem to impact the role of Algeria's newly established energy regulatory agencies (ALNAFT and ARH) and the end of Sonatrach's monopoly ownership and management of pipelines. (Under the amendments, Sonatrach would reserve the right to hold 51 percent of rents derived from pipeline projects.) In his July 15 press conference, Minister of Energy Khelil stressed that "the state supports a fiscal system that anticipates fees, superficial taxes, (and) revenue taxes as much as it maintains an institutional system that supports the separation of the role of the state from the commercial activities of Sonatrach and the transfer of the public powers to the hydrocarbon (regulatory) agencies."

POLITICAL PARTIES AND UNIONS BACK AMENDMENTS

¶6. (U) Algeria's main political parties and trade union federation expressed strong support for the proposed changes to the hydrocarbons law. In a communique issued July 11, the three party presidential coalition backed the changes, noting that they would "ensure a more important rationalization of the country's wealth and give better chances to profit from oil and gas revenues." Louisa Hanoune, the leader of the far-left Workers' Party and the most strident critic of the 2005 law, hailed "this major political decision" as a "new orientation towards the re-nationalization of the country's natural resources." Likewise, a spokesperson for Algeria's trade union federation, the UGTA, expressed July 13 "great satisfaction" with the amendments.

SETBACK FOR ENERGY MINISTER KHELIL

¶7. (SBU) Such amendments come as a setback to Energy Minister Khelil, whose strong advocacy of the 2005 legislation made it come to be known in the Algerian press as "Khelil's law." It is probably not by accident that the recent amendments to the hydrocarbon law were submitted for the President's review by

Finance Minister Medelci while Khelil was traveling in China. Aiming to downplay the modifications, Khelil told the Algerian parliament prior to its recess that "the law has not been changed, but amended." An Embassy contact working for a U.S. energy company told Econoff that he and his colleagues fully expected Khelil to be replaced.

COMMENT

¶8. (SBU) Louisa Hanoune's comments notwithstanding, the proposed amendments to Algeria's hydrocarbon law seem less inspired by Venezuela and Bolivia than by Norway and Kuwait, countries that strategically guarded their energy assets for the benefit of future generations. That being said, and Minister of Energy Khelil's spin aside, Sonatrach's obligatory 51 percent share of new projects as envisioned by the amendments is unquestionably a step back from the spirit of the 2005 law, which sought to transform Sonatrach into a completely independent commercial entity that must compete for Algerian energy projects as any other company.

¶9. (SBU) For his part, Bouteflika reportedly has long been lukewarm about the increased share given to foreign oil companies under the 2005 law. Record-high energy prices and basic arithmetic are probably the driving forces behind the recent changes. Foreign firms operating in Algeria earned USD 4.4 billion in 2005 and they are slated to earn between USD 5 and USD 6 billion this year under the same formulas. Lowering the Sonatrach share to a maximum of 30 percent, while maintaining such a low reference price for the sake of taxation, as Khelil's 2005 law established, translates into even higher revenues for foreign companies at the expense of the Algerian treasury. Bouteflika's recognition of the slow pace of economic reform (reftel) is another likely impetus for amending the law. In a June 25 meeting with the nation's walis (presidentially-appointed regional governors), Bouteflika announced that "today it is our duty to establish the right of future generations to benefit from natural riches. We have come to the conclusion that our generation is not in a position to create an alternative economy from that of hydrocarbons." Establishing a strategic energy reserve would serve as an important hedge against slow (or even bungled) economic reform.

¶10. (SBU) The proposed amendments, while criticized by one Sonatrach executive as imparting a negative image of Algeria to potential investors, would nonetheless likely come as a relief to elements of the Algerian public which were highly critical of the share accorded to foreign investors under the 2005 law and consistently sensitive about the autonomy of foreign energy companies in Algeria. (The Algerian press regularly refers to the oil-producing areas of the south as being like U.S. "states" that are off-limits to Algerians not working for Sonatrach or a foreign oil company.) The Sonatrach executive expressed a degree of shock that the President would so "blindly grope" with such a strategic pillar of the Algerian economy. Foreign oil companies, for their part, appear to be holding their breath as they await implementation of the amendments and their impact on the next round of tenders, slated for the end of the year.

SIEVERS